SURFACE TRANSPORTATION BOARD

Docket No. EP 552 (Sub-No. 16)

RAILROAD REVENUE ADEQUACY—2011 DETERMINATION

Digest:[1] The Board finds that two Class I railroads (Norfolk Southern Combined Railroad Subsidiaries and Union Pacific Railroad Company) are revenue adequate for the year 2011, meaning that two of the Class I railroads achieved a rate of return equal to or greater than the Board's calculation of the average cost of capital to the freight rail industry.

Decided: October 15, 2012

This annual determination of railroad revenue adequacy under 49 U.S.C. § 10704(a)(3) is made in accordance with the standards and procedures developed in Standards for Railroad Revenue Adequacy (Standards I), 364 I.C.C. 803 (1981), Standards for Railroad Revenue Adequacy (Standards II), 3 I.C.C. 2d 261 (1986), and Supplemental Reporting of Consolidated Information for Revenue Adequacy (Supplemental Reporting), 5 I.C.C. 2d 65 (1988). Pursuant to those procedures, which are essentially mechanical, a railroad is considered revenue adequate under 49 U.S.C. § 10704(a) if it achieves a rate of return on net investment (ROI) equal to at least the current cost of capital for the railroad industry.

In Railroad Cost of Capital—2011, EP 558 (Sub-No. 15) (STB served Sept. 13, 2012), we determined that the 2011 railroad industry cost of capital was 11.57%. By comparing this figure to the 2011 ROI data obtained from the carriers' Annual Report R-1 Schedule 250 filings, we have calculated a revenue adequacy figure for each of the Class I freight railroads that were in operation as of December 31, 2011.

A summary of the ROIs for all Class I railroads is set forth in Appendix A to this decision. Appendix B provides the railroads' R-1 Schedule 250 data that was used to compute the ROIs. We find two carriers (Norfolk Southern Combined Railroad Subsidiaries[2] and Union Pacific Railroad Company) to be revenue adequate for 2011 and one carrier (CSX Transportation, Inc.) was very nearly so. Our findings will be final on the effective date of this decision.

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[1] The digest constitutes no part of the decision of the Board but has been prepared for the convenience of the reader. It may not be cited to or relied upon as precedent. Policy Statement on Plain Language Digests in Decisions, EP 696 (STB served Sept. 2, 2010).

[2] Pursuant to Standards I, Standards II, and Supplemental Reporting, revenue adequacy determinations for Class I carriers are made on a system-wide basis, which includes certain railroad affiliates.

This action will not significantly affect either the quality of the human environment or the conservation of energy resources.

It is ordered:

1. This decision is effective October 16, 2012.

2. Notice of this decision will be published in the Federal Register.

By the Board, Chairman Elliott, Vice Chairman Mulvey, and Commissioner Begeman. Vice Chairman Mulvey commented with a separate expression.

VICE CHAIRMAN MULVEY, commenting:

Each year the STB issues a finding on how well the individual railroads have performed in achieving sufficient earnings so that they are “revenue adequate.” Although Class I railroads today are profitable, each year few (if any) are found to be revenue adequate by the Board’s regulatory measure. While this is commonly viewed as an inconsistency, it is important to understand that the Board’s revenue adequacy metric takes into account not only the income sufficient to attract capital, but also the revenue necessary over the long term to maintain and improve the large and costly infrastructure over which railroads operate – the interstate rail network – as well as the costs of locomotives and rolling stock.

APPENDIX A

Railroad	**ROI**
BNSF Railway Company[3]	9.86%
CSX Transportation, Inc.	11.54%
Grand Trunk Corporation (including U.S. affiliates of Canadian National Railway)	8.74%
Kansas City Southern Railway Company	10.76%
Norfolk Southern Combined Railroad Subsidiaries	12.87%
Soo Line Corporation (including U.S. affiliates of Canadian Pacific Railway)	7.13%
Union Pacific Railroad Company	13.11%

[3] BNSF's 2010 and 2011 revenue adequacy calculations are currently at issue in Western Coal Traffic League—Petition for Declaratory Order, Docket No. FD 35506.

APPENDIX B

Railroad	BNSF	CSX	GT	KCS	NS	SOO	UP
Combined/Consolidated Net Railway Operating Income For Reporting Entity	3,273,728	1,883,505	568,033	231,347	1,954,829	193,817	3,474,941
Add: Interest Income from Working Capital Allowance – Cash Portion	303	0	16	453	1,830	93	0
Add: Income Taxes Associated with Non-Rail Income and Deductions	6,751	5,742	16,658	(2)	28,241	(62)	51,353
Add: Gain or (loss) from transfer/reclassification to nonrail-status (net of income taxes)	18,463	(1,052)	1,305	345	21,721	(99)	26,703
**** Adjusted Net Railway Operating Income ****	**3,299,245**	**1,888,195**	**586,012**	**232,143**	**2,006,621**	**193,749**	**3,552,997**
**** Calculating the Adjusted Investment in Railroad Property for the Reporting Entity ****							
Combined Investment in Railroad Property Used in Transportation Service – Ending Balance	48,016,953	23,920,332	9,760,234	2,844,653	23,346,518	3,889,931	38,392,908
Combined Investment in Railroad Property Used in Transportation Service – Beginning Balance	46,300,386	22,927,514	9,433,123	2,572,767	22,141,872	3,703,035	36,912,303
Combined Investment in Railroad Property Used in Transportation Service – Average	**47,158,670**	**23,423,923**	**9,596,679**	**2,708,710**	**22,744,195**	**3,796,483**	**37,652,606**
Other Elements of Investment – Ending Balance	0	0	1,863	0	0	1,135	0
Other Elements of Investment – Beginning Balance	0	0	1,863	0	0	1,135	0
Other Elements of Investment – Average	**0**	**0**	**1,863**	**0**	**0**	**1,135**	**0**
Interest During Construction – Ending Balance	0	0	2,113	4,320	2,580	21,504	43,302
Interest During Construction – Beginning Balance	0	0	2,113	4,320	2,580	21,504	43,309
Interest During Construction – Average	**0**	**0**	**2,113**	**4,320**	**2,580**	**21,504**	**43,306**
Net Rail Assets of Rail Related Affiliates – Ending Balance	331,245	0	143,737	0	0	0	0
Net Rail Assets of Rail Related Affiliates – Beginning Balance	318,021	0	200,443	0	0	0	0
Net Rail Assets of Rail Related Affiliates – Average	**324,633**	**0**	**172,090**	**0**	**0**	**0**	**0**
Working Capital Allowance – Ending Balance	1,032,167	239,548	36,233	73,782	479,292	38,109	971,985
Working Capital Allowance – Beginning Balance	662,693	218,469	51,939	65,931	649,032	86,135	900,106
Working Capital Allowance – Average	**847,430**	**229,009**	**44,086**	**69,857**	**564,162**	**62,122**	**936,046**
Accumulated Deferred Income Tax Credits – Ending Balance	15,520,951	7,576,556	3,217,372	673,659	7,943,800	1,132,870	11,789,873
Accumulated Deferred Income Tax Credits – Beginning Balance	14,219,432	7,010,537	2,985,545	558,326	7,489,154	1,105,164	11,092,135
Accumulated Deferred Income Tax Credits – Average	**14,870,192**	**7,293,547**	**3,101,459**	**615,993**	**7,716,477**	**1,119,017**	**11,441,004**
Tax Adjusted Net Investment Base – Ending Balance	33,859,414	16,583,324	6,718,856	2,240,456	15,879,430	2,772,531	27,531,718
Tax Adjusted Net Investment Base – Beginning Balance	33,061,668	16,135,446	6,695,984	2,076,052	15,299,170	2,661,367	26,676,965
*** Tax Adjusted Net Investment Base ***	**33,460,541**	**16,359,385**	**6,707,420**	**2,158,254**	**15,589,300**	**2,716,949**	**27,104,342**
TAX ADJUSTED RETURN ON INVESTMENT	**9.86%**	**11.54%**	**8.74%**	**10.76%**	**12.87%**	**7.13%**	**13.11%**

The line item descriptions in this schedule are defined in the instructions to the Schedule 250 appearing in Supplemental Reporting of Consolidated Information for Revenue Adequacy Purposes, 5. I.C.C. 2d 65, 80-82 (1988). The Schedule 250 form and instructions are not published in the Code of Federal Regulations.